LIBRARY
SUPREME COURT, U. S.

Supreme Court, U. S.
FILED
JUN 24 1974
MICHAEL RODAK, JR., CLERK

IN THE

Supreme Court of the United States

No. 73 1927

In the Matter of

MARCEL FREUDMANN,

Petitioner,

JOSEPH BLANKSTEIN,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

HAROLD ROSENSTEIN
Attorney for Petitioner
84 William Street
New York, N.Y. 10021

JULIUS ZIZMOR
Of Counsel on the Brief

Dick Bailey Printers • P.O. Box X, Staten Island, N.Y. 10302 • Tel.: (212) 447-5358

TABLE OF CONTENTS

Opinions Below 1

Jurisdiction 2

Jurisdiction and Affirmance Below 2

Questions Presented for Review 2

Statement of Facts Material to the Consideration of the Questions Presented 3

Reasons for Granting Certiorari 9

Basis for Federal Jusisdiction in the Court of First Instance .. 10

Conclusion 10

TABLE OF AUTHORITIES

Halpern v. Schwartz, 426 F.2d 102, 104 (2nd Cir. 1955) 8

Hayslip v. Long, 227 F.2d 550, 553 (5 Cir. 1955) 6,8

Roth v. Fabrikant Bros. Inc., 175 F.2d 665 7,9

STATUTES CITED

11 USC 32(c)(4), Sec. 14(c)(4) 3

28 USC 1254 Sub. 1 2

7 Remington on Bankruptcy (1955) 3157 6

Appendices

A — Judgment of Court of Appeals 12

B — Decision of Court of Appeals 14

C — Decision Re: Discharge 17

D — District Court's Decision 24

E — Decision on Rehearing on Discharge 27

F — Decision of Gurfein J. 35

IN THE
SUPREME COURT OF THE UNITED STATES

October Term, 1973

MARCEL FREUDMANN,

Petitioner,

v.

JOSEPH BLANKSTEIN, Trustee in Bankruptcy

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

Marcel Freudmann, petitioner, for his petition prays that a Writ of Certiorari issue to review the judgment of the U.S. Court of Appeals for the Second Circuit entered herein on March 28, 1974 denying him a discharge in bankruptcy.

OPINIONS BELOW

(a) There are no official or unofficial reports of opinions of the Courts below, except the opinion of the District Court (Gurfein J.) reported in 362 F.Sup.2d 429. The memorandum opinion of the Court of Appeals is not yet reported. It is appended hereto.

JURISDICTION

(b) The grounds on which the jurisdiction of this Court is invoked are found in 28 USC 1254 subdivision 1.

JURISDICTION AND AFFIRMANCE BELOW

(i) The order of the U.S. District Court is dated and entered July 3, 1973 affirming the denial of the bankrupt's discharge. The date of the judgment of the United States Court of Appeals for the Second Circuit is March 28, 1974, entered on that day after argument. A copy is appended. The statutory provision believed to confer on this Court jurisdiction of this appeal is 28 U.S. Code 1254, Subdivision 1.

QUESTIONS PRESENTED FOR REVIEW

1. Was the bankrupt properly denied a discharge in bankruptcy where both the Referee and the District Judge found that the trustee had failed to establish the allegations of Specification of Objection #2, namely, that the bankrupt had made a fraudulent transfer of his property by selling merchandise for cash for an inadequate consideration. *Per contra* the Court found that there was an absence of proof that the transfer was for less than a fair or adequate consideration.

2. Do the facts presented in this record establish intent to defraud — a necessary ingredient to bar a discharge, where the Court found that the bankrupt used the proceeds realized on the sale of the merchandise to pay his legitimate creditors, and the trustee failed to establish that any sale was for less than fair consideration?

STATEMENT OF FACTS MATERIAL TO THE CONSIDERATION OF THE QUESTIONS PRESENTED

The bankrupt's discharge has been denied on grounds which basically are not set forth in the Bankruptcy Act. Indeed, the District Court, in upholding the extraordinary denial of the discharge conceded that no reported case sanctions such denial. Thus, at A-43 it said:

> "There is no authority cited by the distinguished Referee or by the parties which is directly in point."

The Court of Appeals, in affirming the District Court, also failed to cite any authority in support of its determination. In a word, the bankrupt's discharge has been barred upon a factual situation never approved by any Federal Court. This in itself should warrant that certiorari be granted.

The bankrupt, a diamond merchant, was engaged in business for many years. The trustee filed multiple objections to his discharge. All were dismissed and/or withdrawn save number two,* the relevant portion of which reads:

."1. Section 14(c)(4) of the Bankruptcy Act 11, U.S.C. 32(c)(4) provides:

> (c) the court shall grant the discharge unless satisfied that the bankrupt has . . . (4) at any time subsequent to the first day of the twelve months immediately preceding the filing of the petition in bankruptcy, transferred, removed, destroyed, or concealed, or permitted to be removed, destroyed, or concealed, any of his property, with intent to hinder, delay, or defraud his creditors."

"That on and after May 29, 1969, subsequent to the first day of the 12 months immediately preceding the filing of the petition the bankrupt transferred certain of his property, to wit, diamonds to [certain persons] . . . for an inadequate consideration with intent to hinder, delay or defraud his creditors."

The referee sustained this objection and denied the discharge. After several reviews, the District Court (Gurfein J.), confirmed the determination although he found that the bankrupt deposited all funds received from the "transfers" in his bank account and used them to pay notes held by his trade creditors, that no proof was offered that any transfer was made for less than fair value (A-44) or for an inadequate consideration (A-46). Nonetheless he denied the bankrupt's discharge, and strangely concluded that even though proof of wrong doing was lacking, the bankrupt was guilty of intent to defraud! The Court said:

"*While I cannot find that there is aaequate proof in this record that the cash sales were 'without fair consideration.*' it is my opinion that the evidence adequately supports Referee Herzog's ultimate finding that the bankrupt actually intended to defraud his creditors by fraudulent transfers."

The predicate for the extraordinary finding of intent to defraud in face of the exculpatory facts herein, stems from the following circumstances: The bankrupt was in financial difficulties for more than a year prior to bankruptcy and in need of cash. During the period he bought diamonds on long term credit from different vendors and in fifteen different instances, almost immediately sold the merchandise at a loss for cash to various buyers (some of whom were his creditors) because of his

urgent need to meet other obligations to trade creditors. As indicated, Gurfein J. found that all the monies received were deposited by the bankrupt in his business account and used to pay creditors (A-40). Indeed, Judge Gurfein found the facts which wholly vindicate the bankrupt and declare his entitlement to a discharge. He stated:

"(a) no sales were made of merchandise held on memorandum: (b) all purchases were made on long-term credit at prices which were obviously considerably above the market prices; (c) in at least seven transactions the vendors or creditors were paid in full prior to the bankruptcy proceedings; (d) in two instances of the seven paid-in-full transactions the transactions occurred more than a year before bankruptcy; (e) in three instances payments on account were made; and (f) in the remaining transactions no payments were made because when the payments became due the bankrupt had already ceased doing business or bankruptcy proceedings had been instituted.

The Referee substantially found all these facts, except that he did not find either way on the point that the purchase prices paid by the bankrupt were 'obviously' considerably above the market price."

Judge Gurfein continued:

"Cash sales of property by the debtor are not prohibited whether made for the purpose of meeting an indebtedness or in the ordinary course of business. Cash sales are clearly transfers but the existence of any fraudulent intent to put property beyond the reach of creditors is strongly negated by the receipt of cash. 1 Collier 3.102[2] (footnotes omitted).

Where the claim is that a transfer was made with intent

to defraud creditors, the transfer may be shown to have been made for an inadequate consideration. 7*Remington On Bankruptcy* (1955) 3157. But merely selling inventory below cost to meet maturing debts would not be a transfer with intent to hinder, delay or defraud creditors, as Referee Herzog stated. So, too, if the bankrupt had merely taken diamonds he purchased and given them to a creditor for payment of an antecedent debt that would have amounted to a preference but not necessarily to a fraudulent conveyance. *Hayslip* v. *Long*, 227 F.2d 550, 553 (5 Cir. 1955). Here, the debtor sold the diamonds and used the proceeds rather than the diamonds themselves to prefer the credit. . . .

If the essence of the fraud is the sale for an inadequate consideration, the objective inadequacy of the consideration paid by the purchaser to the bankrupt has not been proved. In a market like the wholesale diamond market there must, of necessity, be at least two prices, one for sales on credit, the other for cash sales. The former must include what is in effect a premium for credit insurance. How large the spread should be is not disclosed in the record. Moreover, diamonds are not fungible in quality and one man's judgment does not always coincide with another's respecting the value of a particular parcel of diamonds. This means that after the diamonds are dispersed it is hard to get an expert opinion on market price except for certain standard sizes.

The man who buys for cash and sells on time can sometimes make some profit because of the differing terms of sale. It does not work the other way. *There is no proof, however, that the bankrupt sold for prices that were*

> ***objectively not fair consideration, for the fair price on a cash purchase may have been no more than what Freudmann got for the goods.*** What Freudmann paid for the goods himself may have been an excessive price which he was willing to pay to get the goods in his hands for conversion to needed cash. He may actually have sold for an adequate cash price on the market, though for him it was a sale at a loss. Cf. *Roth* v. *Fabrikant Bros. Inc.*, 175 F.2d 665, 667-68 (2 Cir. 1949; discussion of this problem by Judge A. N. Hand)."

Of the fifteen creditors discussed in the Referee's and District Court decision, a number of them bought the diamonds from the bankrupt at a loss to him; seven were fully paid by the bankrupt; two of the transactions occurred more than one year prior to bankruptcy. In three instances, payments on account were made to the creditors by the bankrupt which wholly negated any claim of intent to defraud.

The prime contention of the Referee, Judge Gurfein, and the Court below, was that the bankrupt was guilty of intent to defraud because "at the end of the line", i.e., when he was petitioned into bankruptcy in 1970, certain "end creditors" were not paid. However, this is true in every bankruptcy and those "at the end of the line" suffer loss. Nonetheless, intent to defraud was wholly demolished by Judge Gurfein's own findings that the diamonds were *not* sold by the bankrupt at an inadequate price or without fair consideration, and that all monies received therefor were deposited in his business account and used to pay merchandise creditors, the hallmark of a legitimate transfer. See *Roth v. Fabrikant Bros.*, 175 F.2d 665 (2nd Cir.). The estate was not depleted by the bankrupt's acts, nor have the rights of creditors been prejudiced where the bankrupt used the funds to pay his debts to them.

There is no ground set forth in the bankruptcy act for barring a discharge to a person who buys merchandise on long term credit, then resells it for cash at a lower but legitimate price, and uses the proceeds thereof to pay his pressing debts. Judge Gurfein in his opinion, *supra,* found this to be the fact and the law. The very essence of specification Two was the allegation that the merchandise was sold and/or transferred for an *inadequate consideration* with intent to defraud creditors. Yet, Judge Gurfein found that there was no proof of inadequate consideration or that any sale was made for less than a fair consideration. Similarly, while the referee characterized the bankrupt's actions as "a ponzi or a kiting scheme", nonetheless, there is no proof that any of the fifteen sales discussed were for an unfair or inadequate consideration. In a word, the specification as alleged was unproved. In these circumstances, there was no basis for denying a discharge under any provision of the Bankruptcy Act. To bar a discharge, *actual,* not constructive fraud must be proved. *Halpern v. Schwartz,* 426 F.2d 102, 104 (2nd Cir. 1970).

A preferential transfer or payment does not bar a discharge under the Bankruptcy Act, *Hayslip v. Long,* 227 F.2d 550, 553 (5th Cir. 1955).

The fact the bankrupt used the funds realized by him from the sales to pay creditors, clearly indicates that he rebutted any presumption of fraud which may have been cast upon him by law. The finding that the trustee failed to establish that the merchandise was sold for less than fair value and/or for an inadequate consideration demolished the specification as pleaded and mandated that a discharge issue.

REASONS FOR GRANTING CERTIORARI

(1) The District Court (Gurfein J.) in affirming the denial of the discharge in the absence of proof of inadequate consideration, specifically stated that no Federal Court decision exists which sanctions the denial thereof in the factual spectrum here outlined. Moreover, such denial is contrary to the Second Circuit's ruling in *Roth v. Fabrikant Bros.*, 175 Fed. 2d 665, and the provisions of the Bankruptcy Act. The Court of Appeals cited no authority for its affirmance at bar.

(2) The bankrupt has been denied a discharge on the ground that he made transfers of his property with intent to defraud, yet the Court found that the trustee failed to establish that a sale or transfer was made without adequate, proper or fair consideration and that the proceeds realized were used by the bankrupt to pay his creditors. The right to a discharge is of transcendant importance and the questions here asserted should be settled by this Court to determine this important Federal question which has been improperly decided.

(3) An important aspect of the Bankruptcy Act relating to the bankrupt's right to a discharge which is of national importance, has been decided by the Court of Appeals for the Second Circuit, the District Court and the Referee, contrary to law and has so far departed from the accepted and usual court of judicial rulings in bankruptcy that it calls for an exercise of this Court's power of supervision and reversal.

BASIS FOR FEDERAL JURISDICTION IN THE COURT OF FIRST INSTANCE

The jurisdiction is founded on the provisions of the Bankruptcy Court which vests the Federal Court with sole and exclusive jurisdiction in bankruptcy matters and those relating to a discharge.

CONCLUSION

FOR THESE REASONS, STATED ABOVE, IT IS PRAYED THAT A WRIT OF CERTIORARI ISSUE TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT TO REVIEW ITS AFFIRMANCE OF THE ORDER OF THE UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF NEW YORK AFFIRMING THE REFEREE'S DECISION DENYING THE BANKRUPT A DISCHARGE.

Respectfully submitted,

HAROLD ROSENSTEIN
Attorney for Petitioner

JULIUS ZIZMOR
Of Counsel on the Petition